

FINAL TASK ORDER REPORT

MARCH 2004 TO NOVEMBER 2005

**SOUTH AFRICA:
CAPITAL & FINANCING STRATEGIES
FOR MUNICIPALITIES**

Prepared for



Prepared by

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FINAL TASK ORDER REPORT

SOUTH AFRICA: CAPITAL & FINANCING STRATEGIES FOR MUNICIPALITIES MANGAUNG LOCAL MUNICIPALITY POLOKWANE LOCAL MUNICIPALITY TSHWANE METROPOLITAN MUNICIPALITY

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TASK ORDER DESCRIPTION

The purpose of the project was to assist the Tshwane, Mangaung and Polokwane Municipalities to develop 10 – 20 year capital improvement and financing strategies. The basic methodology was to work with the municipal manager and staff in participating municipalities to develop clear strategic choices for the municipal council's consideration. This long-range planning process was integrated with each municipality's financial and physical planning processes, and should inform both the Integrated Development Plan required by the Municipal Systems Act and the three-year budget processes required by the Municipal Finance Management Act

The project worked with several municipalities to develop the in-house institutional and human resource capacity to revise and update the capital and financing strategy on an ongoing basis. The consultant's ensured that a team of municipal officials within each municipality knows and understands the details of the methodology are capable of building on the initial work and replicating it in others. The international advisors funded by National Treasury assisted in ensuring that this project was integrated with the finance reform process currently being carried out in these municipalities.

I. OVERVIEW OF PROJECT HIGHLIGHTS

The following give a chronological breakdown of key moments in the progress of the project:

March 2004 to June 2004

- The contract between UI and USAID was signed on March 1, 2004.

- Local contracts with consultants completed.
- Project management arrangements and operational procedures established.
- Operational contact established with USAID.
- First project team meeting held.
- Working relationships with SANT agreed upon.
- Documents to introduce the project to the three cities were drafted.
- Initial data scan on the three sites were done.
- First contact with cities initiated.

July 2004 to September 2004

- The completion of the initiation phase of the project according to schedule which entailed:
 - The introduction of the project to the senior management and politicians of the three cities.
 - The finalization of project steering committees in each city.
 - At least three visits to each city.
 - Memorandum of Understanding was drafted and distributed for comments.
- Starting with the second phase of the project which aims at building a picture of the strategic and operational environments for the purposes of this project.

October 2004 to December 2004

- First stakeholder meeting.
- Project moved into operational phase.
- Interaction with cities became more routine and at an operational level.
- Dr Peterson visited the country and each city involved in the project.
- Information gathering commenced with all three Municipalities.
- Second stakeholder workshop on 1 December 2004.
- Next round of meetings at senior management level immediately before and after the stakeholder workshop.

January 2005 to March 2005

- Continuing with "Building the big picture". First round data gathering completed.
- Launching the project web site by the second week of October 2004.
- Build the model for a first round of infrastructure investment modeling.
- Completion of first round modeling for each of the cities.
- Intensified operational contact with each of the Councils.

April 2005 to June 2005

- The modeling was finalized
- A module for quantifying economic and labor impact was added
- Presentations was done to the executive management of all three Councils
- Key policy issues were confirmed
- Investment scenarios were developed for each Council
- Dr Peterson visited South Africa
- Completion of all technical work
- Drafting of reports



July 2005 to September 2005

- Finalization of reports
- Visit by Dr Peterson to South Africa
- Working documents and final strategy report from the team was handed to all councils with requests for comments
- First debriefing with USAID/SANT

September 2005 to November 2005

- Final stakeholder meeting
- Council took the reports through their committee systems to Council
- Final debriefing with USAID

II. PROGRESS OF MAJOR ACTIVITIES

Meeting and liaison with USAID

Meetings and liaison with USAID took place as a matter of routine. The USAID representative on the project was invited to the more important strategic meetings between the team and the Council as per agreement, reached with USAID exception reporting remained the basis for interaction and communications. All relevant correspondence was forwarded to USAID for their information.

Project management

Project management continued as indicated in the previous report. Regular operational interaction took place between team members. Monthly project team meetings were held and the proceedings, discussions and resolutions were recorded and distributed to the team members.

Stakeholder interaction and involvement

Stakeholder interaction took place on an ad hoc basis. DBSA maintained an active role in the project as indicated as part of the project plan.

Interaction with the three Councils involved

Interactions with the councils differ according to local circumstances. The team was led by local protocols and there was therefore a different approach for each Council. It is important to note that the SOW indicated a preferred working method but this was not always possible. Working relationships with all councils were good. The team maintained formal and informal contact as many times as possible. This was necessary in order to maintain the momentum during the life of the project.

III. DELIVERABLES AND REPORTS I.T.O. THE SOW

Statement of work as per Contract	Issues addressed	Deliverables
<p>Phase 1: Effective buy-in:</p> <p>It will be important to get the buy in of the Mayor's; Council's; National Treasury; and the South African Cities Network's at the onset, and to establish a working relationship with a committee of Council as agreed with the municipality's political leadership. It will also be critical to secure the constructive participation of the municipal manager, chief financial officer, planning staff, public works staff, National Treasury team and South Africa Cities Network project manager.</p> <ul style="list-style-type: none"> The Contractor will work with the Mayor and or the Mayoral Committee and Portfolio Committees appropriate in each municipality, and with the Municipal Manager and appropriate senior management official(s) to secure their commitment to the project. The Contractor will work with the municipality to develop a memorandum of understanding, to be signed by the municipality and USAID that will specify: <ul style="list-style-type: none"> Which member(s) or structure(s) of the municipal council will be primarily responsible for supervising the project and managing the council's relationship with the project. Which member(s) and structure(s) of municipal staff will be primarily responsible for implementation of the project and integration of the project into the municipality's planning and financial systems. Required inputs from the Council and staff, in terms of time, information, personnel, and physical facilities. Expected outputs from the project, including staff development and capacity building, periodic reports, a timeline, milestones, computer models, policy analysis, and key decision points for the council. Expected linkages between the capital and financing strategy and the municipality's IDP and budget processes. Responsibility for updating the capital and financing strategy in future 	<p>Inception phase</p> <p>During the inception phase the key objective was to get buy-in and support from each Council. This was done through:</p> <ul style="list-style-type: none"> <i>Developing a clear understanding of what the project will deliver.</i> It was important that political leaders and management shared the same expectations as to project outputs. This was done in order to avoid a discrepancy between the two that might have raised tensions in implementation. Short informal sessions with key role players were held to gain an understanding of sensitivities and issues in each Council. The team ensured that all concepts, issues and processes involved in the work program were clearly understood before implementation started. Critical decisions to be made in the course of the work program were identified and agreed upon by all involved. Links with the core planning and budgeting process of the Council were established. These linkages influenced the detailed scheduling of the project, in order to allow the benefits of the project to inform parallel budget processes at critical junctures. 	<p>Two key deliverables resulted from this phase:</p> <ul style="list-style-type: none"> A detailed inception plan prepared by the consultants that served as operational blue print for the project. A clear and common understanding of the project in terms of approach, methodology and deliverables.
<p>Phase 2: "Big Picture" options:</p> <p><i>1. Preliminary options</i></p> <p>The Contractor will work with the municipality's management team to develop several "big-picture" 10 – 20 year strategic options for Council's consideration.</p> <p>Key inputs at this stage will be existing data concerning infrastructure needed within the municipality and the condition of existing assets and schedules for their replacement or rehabilitation. If adequate data is not available to develop the preliminary options, this gap should be identified as soon as possible, and a remedial plan developed, in consultation with the municipality, to develop usable data. A process may need to be implemented, depending on each municipality, to quantify and assess current service levels, standards, backlogs, and growth expectations. The remainder of the project may need to be delayed until such data has been</p>	<p>Big Picture – first cut</p> <p>During this phase the consultants facilitated a process whereby a clear picture was built of the all the factors affecting infrastructure investment and capital budgeting. Existing information was used. The assessment will covered:</p> <ul style="list-style-type: none"> The socio-economic environment of the population and non-residential service demands. The services environment and the status quo regarding provision of each of the five major infrastructure services. Specific attention was paid to service levels as the most 	<p>The completion of this phase resulted in:</p> <ul style="list-style-type: none"> A primary data profile of the municipality. Where possible, data was presented in such a way that they could be linked to the Council's GIS system. Since an existing model was used, this phase was used to structure the model and to setup the modules to suit local circumstances.



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<p>developed.</p> <p>Preliminary strategic options:</p> <ul style="list-style-type: none"> ▪ Should be described in narrative form, modeled on MS Excel spreadsheets, and represented graphically ▪ Should be based on at least three different resource-mobilization scenarios (more or less progressive approaches to taxes, tariffs, and borrowing) and at least three different spending scenarios (with varying emphasis on rehabilitating existing physical plant, extending new infrastructure, and strategic economic development investment). ▪ Should include indicative estimates of capital cost, borrowing costs, increased or decreased operating costs, and increased or decreased operating revenues ▪ Should include one or more key indicators of the investment mix needed and its impact on private sector investment, economic growth, and employment. ▪ Should cover a wide enough range to demonstrate, <u>to the extent that it is feasible</u>, meaningful differences in the way the municipality will look and feel at the end of the planning horizon under each option, addressing issues such as: <ul style="list-style-type: none"> ○ If municipalities continue spending at x level: <ul style="list-style-type: none"> ▪ What will be the condition of current infrastructure in 10 - 20 years? ▪ How much private investment will have been leveraged in, or foregone because services were not available to support development? ▪ How many unserved or underserved people and dwellings will still be without adequate services? ▪ What will revenues be? ▪ What will taxes and tariffs be? ○ What effect do the spending mix and borrowing levels have on: <ul style="list-style-type: none"> ▪ Service levels? ▪ Employment opportunities? ▪ Financial sustainability of the municipality? ▪ Economic activity in the municipality? 	<p>critical issue affecting long-term financial sustainability.</p> <ul style="list-style-type: none"> ▪ The financial position of the Council. <p>These issues were dealt with in a qualitative and quantitative way. Substantial time was spent verifying and validating key data. Important issues regarding current service delivery standards and financing were clarified in the process of data reconciliation. The key benefit of spending time on this phase is that it increased the understanding of basic relationships and issues by local politicians and administrators. After the initial scan, the municipal picture was clearer and local circumstances could be accommodated in the work plan.</p>	
<p>2. Presentations and feedback</p> <p>With the guidance of the member(s) of Council responsible for supervising the project, the Contractor and</p>	<p>Big picture: Formal presentation to political leadership</p> <p>A number of events took place before this phase could reach its goal of intensive interaction with the political leadership.</p>	<p>The following deliverable resulted from this phase:</p> <ul style="list-style-type: none"> • A fully calibrated model

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<p>management team will devise appropriate mechanisms for presenting the preliminary options to Councils and to relevant executive or council committees, and to members of the community, community-based and non-governmental organizations, and business groups.</p> <ul style="list-style-type: none"> Comments and submissions received at committee and Council meetings, and in each public forum should be documented and summarized. Summaries should be circulated to members of Council as may be agreed with the member(s) responsible for supervising the project. 	<ul style="list-style-type: none"> The first priority during this phase was to calibrate the model to reflect the base year of assessment as closely as possible. Parameters (which could be modified) were established for external growth rates, future inflation etc. Several key questions were resolved at this stage. <ul style="list-style-type: none"> What type of service is appropriate and practical in the area? Discussion with officials will play an important role in identifying service expectations. What timeframes should the team consider in addressing certain critical issues such as the eradication of backlogs? Which "what if" scenarios will be used in preparation for the workshop with politicians? These "what-ifs" are important because they are used to illustrate the implications of certain political choices and preferences. A number of scenarios were prepared for the workshops. These scenarios were based on (i) political preferences for service delivery (typically, ambitious levels), (ii) the implications of meeting the minimum requirements of Government policy, and (iii) the implications of an option where service levels are aligned with household incomes in order to resolve some affordability issues. It was possible to build further scenarios on an interactive basis with the councils. This was the preferred route and some principles could be demonstrated in this way. The last step of this phase was to use the workshop to build consensus on certain key choices and policy parameters that must be reflected in the final strategy to be developed. 	<p>with key scenarios prepared.</p> <ul style="list-style-type: none"> An interim report showing the options and policy choices the Council is confronted with. Policy parameters for capital budgeting and funding strategies. A list of risk factors for investment and service delivery and the extent to which they can affect service delivery and capital budgeting.
<p>3. <i>Final options</i></p> <p>Relevant comments and submissions should be taken into</p>	<p>Big picture: selection of option</p> <p>The main activity in this phase was to select the appropriate strategic</p>	<p>This phase of the project</p>



Statement of work as per Contract	Issues addressed	Deliverables
<p>consideration, and the options should be revised and refined as appropriate.</p> <p>With the guidance of the member(s) of Council responsible for supervising the project, a final set of options should be presented to council for discussion and direction on which option or combination of options should be developed into the municipality's capital and financing strategy.</p>	<p>option. The steps were:</p> <ul style="list-style-type: none">▪ Development of the final strategic option, that was the basis for the final modeling.▪ Linking the strategic option back into the core processes of the Council. This included spelling out the consequences for the IDP, LED and budget processes of the Council▪ Identification of the parameters for project prioritization and capital budgeting.	<p>delivered a final model and a final draft strategy document for the Council to consider, together with recommendations about linkages to other Council processes.</p>
<p>Phase 3: The strategy document and capital/financing model</p> <p>Following the Councils' selection of a preferred option, the Contractor and the municipality's management team should develop a capital improvement and financing strategy document, which details the municipality's long-range strategy.</p> <p>With the guidance of the member(s) of Council responsible for supervising the project, the strategy should be formally presented to the municipal Council for discussion and adoption. The strategy document should include narrative, tables, and graphs which:</p> <ul style="list-style-type: none">• show estimated capital cost of the planned projects, together with borrowing costs, increases or decreases to operating costs, and increases or decreases to operating revenues resulting from the projects• identify the tax, tariff and borrowing policies that the municipality intends to pursue in order to mobilise the necessary resources• identify indicative tax, tariff, and debt levels for each year to the planning horizon• clearly state how investment resources will be allocated along between competing objectives (e.g. capital rehab, service extension, and economic development)• provide sufficient specificity on projects to allow project feasibility and design work to move forward in a timely fashion. This implies greater specificity for early years, and more conceptual project identification for outer years• identify target spending levels and allocation to projects and/or objectives for each year to the planning horizon• identify target levels for private sector investment, economic growth, and employment over the strategy period.• provide a suggested methodology and timetable for updating the long term capital infrastructure and financing strategy every 3 – 5 years, to evaluate implementation to date, revise as needed, add additional years to the planning horizon as needed,	<p>Final strategy</p> <p>The main activity in this phase was presentation of the strategies to the Councils. The presentation contained recommendations regarding the way forward. The way forward spell out:</p> <ul style="list-style-type: none">▪ Performance criteria to assess the success of the Council with strategy implementation.	<p>The deliverables were:</p> <ul style="list-style-type: none">▪ A final presentation to the Council

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<p>and provide increased specificity for smooth planning and procurement.</p> <p>After Council discussion, the strategy document will be revised and refined as appropriate.</p> <p>When the Council is satisfied with the strategy document, it should be adopted by resolution of the Council.</p> <p>Each municipality will be assisted in the development of a spreadsheet model that can readily be updated each year, in connection with the IDP and budget processes. This model should enable the municipality to annually produce a revised capital and financing strategy using their own personnel and data. Success will be based on completion and intelligence of the model.</p>		

VI. LESSONS LEARNED AND ISSUES TO BE NOTED

The project was complicated and crossed boundaries between functional and strategic activities in the Councils. The following observations are regarded as relevant and should be noted:

Strategy Documents

The preparation of strategy documents with the assistance of external consultants underlined the fact that projects of this nature cannot formulate strategy for a Council. It can at best facilitate and inform the process. This is illustrated best by the way in which Tshwane dealt with the strategy document developed with the assistance of the project team. Mangaung and Tshwane have taken the document to council while in Polokwane process is still unclear. According to informal feedback, in Tshwane, the strategy was presented to the Mayoral Committee with internally formulated recommendations. The report was approved and submitted to Council where the ruling party withdrew it from the agenda. No further information is available.

General Point/Observations

The following observations are based on the experience of the project team.

Polokwane

- Cooperation with the Council at all levels was good.
- Continuity in Polokwane became a problem from time to time. Key persons involved changed during the project implementation.
- Responses from the Council were often slow.
- Polokwane often demonstrated the best insight of all councils into the issues at stake.
- The final analysis showed that Polokwane has financial potential to sustain service delivery under existing national policy conditions but are constrained in terms of institutional capacity to implement and sustain service delivery.

Tshwane



- Urban Institute developed a good working relationship with the Council at all levels.
- More than 80 meeting were held with officials at strategic and operational level.
- As is the case in all councils, there seems to be a substantial gap in the Council between strategic and operational levels. There is not always an appreciation of the problems and challenges across this divide. Furthermore, there are still strong indications that sector departments tend to operate in functional compartments with little horizontal integration of operational activities.
- Very specific recommendations were made in the final internal submission to Council, including on issues as revisiting the Council's tariff policy. However, the team does not know the content of these recommendations.
- The project clearly pointed out that the Council will have to put a lot of emphasis on demand management.
- Tshwane's major challenge is to cope with growth and not addressing backlogs. However, a strategy that fails to address growth will result in unmanageable service backlogs.
- Tshwane seems to have strong institutional capacity but indications are that their financial capacity is very close to its limits. Ad hoc and prestige capital projects that do not have full cost recovery are a serious risk to the future sustainability of the Council.

Mangaung

- Mangaung has progressed well at various levels of strategy and policy formulation. This was a benefit to the project and helped to contextualize the project activities.
- There still seems to be conflict as to the future integration and responsibilities regarding the outcomes of the project. However, subsequent feedback indicated that this matter might be resolved in the near future.
- The Council is also limited in its financial capacity although general institutional capacity is good. However, the Council, like all the councils, is very vulnerable to changes in the national policy environment. Demands from national departments such as DWAF on the eradication of backlogs and the lack of an infrastructure component linked to the housing subsidies, puts this and the other Councils at risk. One cannot allow untested national policy directives to destabilize local government.

General

The following general observations can be made:

- Municipalities need to borrow in order to address backlogs. Achieving service delivery targets is dependent on substantial borrowing in all instances. The inability to create and sustain a viable borrowing environment in local government is going to prevent national government from achieving its service delivery targets. Borrowing as funding source of capital budgets has decreased in contribution over the past years and has largely been substituted by subsidies. Real capital expenditure is decreasing instead of increasing when municipal budgets are compared over time.
- The debt carrying capacity of municipalities is not bad and there seems to be substantial room for borrowing. However, the borrowing capacity municipalities are constrained by the inability to raise the necessary operating income to service loans and to operate and maintain the assets created in the process. The impact of capital subsidies in the operations of Councils is further limiting the ability of councils to raise the necessary funds through borrowing.
- The general quality and credibility of information at municipal level is very poor. Data is generated in an ad hoc manner, not integrated and incomplete. It undermines any planning and decision making.

- The project has resulted in improved horizontal communication between line departments of municipalities.
- Capacity in municipalities is limited. However, it seems the extent of demand for compliance in various issues from national departments is sometime constraining the ability to focus on the tasks at hand. This applies to deadlines for SANT submissions, budget programs, IDP timeframes, deadlines for submitting WSDP, MIG business plans, etc.
- The project delivered a strategy document relatively close to the end of the project. However, it seems more appropriate to put a draft and even controversial strategy document on the table as early as possible. This clearly stimulates interest and debate. It seems that the councils and officials found it difficult to get involved at conceptual stage and to make concrete and relevant inputs at that stage. A draft strategy should not be presented later than two thirds through the process.
- The distance factor played a role in the process – It was not possible and practical to develop the same level and intensity of involvement with Mangaung and Polokwane as was the case with Tshwane.
- Although the project delivered a strategy there is clearly a need to support the Councils with implementation. The “what now?” questions remain.
- The project was limited to certain scenarios and therefore there was limited debate on certain issues.
- National government clearly creates expectations through policy statements, which the municipalities cannot implement. This puts local councils under pressure and creates tension between the Council and its constituencies.

Follow-up

- The model used during the project was provided to the councils on request. However, given the complexity of the model, it is doubtful if they will make any sense out of it. The model was regarded as a problem-solving tool by the team and not an end in itself. The model was given to Polokwane (Jim Hewitt) and will also be made available to Mangaung.
- There seems to be substantial interest in the process and the needs for infrastructure investment planning is generally accepted and understood. However, there is no source for funding technical assistance currently to assist municipalities in this regard. On the initiative of one of the subcontractors, discussions are currently taking place with Gauteng Province on a provincial infrastructure investment framework as well as with Bojanala Platinum (Rustenburg LM) and Gert Sibande District Municipalities.